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From:

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To:

Cc:

Subject: RE: Application of 6707A in DATs

Scenario 1

1) For transactions listed after a taxpayer has filed a return reflecting the benefits of the transaction, the Form 8886 and the 6011 regulations do not require the taxpayer to identify each year in which the taxpayer participated in that transaction. In the past, when a taxpayer has failed to disclose on the next filed return his participation in previous years, we assessed only one penalty - not a separate penalty for each tax year in which there was participation. In keeping with that practice of "one penalty per required disclosure form," we believe the best course to calculate the penalty in your first scenario is to add the decrease in tax shown on each year's return (for and) to reach the total tax decrease covered by the single required disclosure. After taking 75% of that amount, the maximum and minimum rules should be applied to determine the penalty.

2) The decrease used in calculating the penalty is the decrease in tax shown on the return as filed. It does not matter whether the claimed decrease is allowed or disallowed or settled in some manner between the two. The penalty would apply for failure to disclose even if the transaction is valid. The return would still show a tax decrease resulting from a valid reportable transaction and that decrease is the amount used in calculating the section 6707A penalty.

Scenario 2

1) and 2). We concur in the advice you propose. Seventy-five percent of the total amount of the decrease in tax for through , when the disclosure was required, is more than the maximum penalty allowed, so the penalty will be the maximum of \$100,000 for . The penalty for will be 75% of the decrease in tax shown on the return, which is less than the minimum amount, so that the penalty for will be the \$5,000 minimum amount..

Scenario 3

The penalty for the failure to disclose is calculated on the decrease in tax shown on the return of the entity that participated in the transaction. A subchapter S corporation generally does not have an income tax liability, and thus, its return does not reflect a decrease in tax. Hence, the section 6707A penalty on the subchapter S corporation for the year is the statutory minimum of \$10,000. The C corporation that goes out of existence never files (and is not required to file) a return subsequent to the listing of the transaction in which it engaged and, therefore, never had an obligation to make a disclosure.